STATE OF MICHIGAN
IN THE SUPREME COURT

GRASS LAKE IMPROVEMENT BOARD	Supreme Court No. 154364
Petitioner-Appellant	Court of Appeals No. 326571
v	Ingham Circuit Court No. 2014-1064-AA
MICHIGAN DEPARTMENT OF ENVIRONMENTAL QUALITY	MAHS Case No. 09-63-0026-P
Respondent-Appellee	

_____/

MICHIGAN DEPARTMENT OF ENVIRONMENTAL QUALITY'S BRIEF IN OPPOSITION TO THE GRASS LAKE IMPROVEMENT BOARD'S APPLICATION FOR LEAVE TO APPEAL

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1. Under the Administrative Procedures Act, the prevailing party in a contested case hearing may recover attorney fees if the administrative law judge finds that the agency's position was frivolous because it "was devoid of *arguable* legal merit." MCL 24.323(1)(c) (emphasis added). This matter involves a clear conflict between a statute and rule, in which the application of each necessitated opposite results. Did the Court of Appeals correctly hold that the Department of Environmental Quality's position in the underlying contested case – that it should apply the statute until it could change the rule – was sufficiently grounded in law as to have at least some arguable merit, and hence it was not frivolous under MCL 24.323(1)(c)?

   Appellant's answer: No.

   Appellee's answer: Yes.

   Trial court's answer: No.

   Court of Appeals' answer: Yes.

2. Here, on direct appeal, the circuit court relied upon an incorrect procedural statute and held that the Department of Environmental Quality's position was "devoid of legal merit," and on that basis reversed the administrative law judge's decision denying attorney fees. Did the Court of Appeals properly conclude that the circuit court applied incorrect legal principles and reinstate the administrative decision?

   Appellant's answer: No.

   Appellee's answer: Yes.

   Trial court's answer: Did not answer.

   Court of Appeals' answer: Yes.

STATUTES AND REGULATIONS INVOLVED

MCL 324.30102(1)(d)

> Except as provided in this part, a person without a permit from the department shall not do any of the following:
>
> . . . .
>
> (d) Create, enlarge, or diminish an inland lake or stream.

Mich Admin Code, R 281.811(1)(e)[1]

> "Enlarge or diminish an inland lake or stream" means the dredging or filling of bottomlands, or the dredging of adjacent shorelands, to increase or decrease a body of water's surface area or storage capacity or the placement of fill or structures, or the manipulation, operation, or removal of fill or structures, to increase or decrease water levels in a lake, stream, or impoundment.

[1] Mich Admin Code, R 281.811(1)(e) has since been amended, and this definition has been removed. 2015 Michigan Register 5 (April 1, 2015), p 75. The version provided here is the rule as it existed when this litigation arose.

COUNTER-STATEMENT OF JURISDICTION

The Michigan Court of Appeals issued its opinion on July 21, 2016, which reversed the Ingham Circuit Court's opinion and order, and reinstated the decision of the Administrative Law Judge denying the Grass Lake Improvement Board's petition for attorney fees. The Court of Appeals held that the circuit court applied incorrect legal principles and that the administrative law judge did not abuse his discretion in determining that the Michigan Department of Environmental Quality's position in the underlying contested case was not devoid of arguable legal merit. The Grass Lake Improvement Board now seeks leave to appeal, pursuant to MCL 600.232 and MCR 7.305, from the Court of Appeals' opinion.

INTRODUCTION

This case is not jurisprudentially significant and does not otherwise merit review by this Court. It arises from a narrow dispute involving a petition for attorney fees under the Administrative Procedures Act and whether the Department of Environmental Quality's legal position in a single contested case hearing on a permit application was "devoid of arguable legal merit," and therefore "frivolous" within the meaning of MCL 24.323(1). The specific context of the dispute was an apparent or, at a minimum, arguable conflict between a statute and a now-superseded administrative rule.

The Grass Lake Improvement Board (Lake Board) applied for a permit to construct an augmentation well that would extract groundwater and pump it into Grass Lake, in Oakland County, to raise the lake level. The statute at issue, Part 301, Inland Lakes and Streams, of the Natural Resources and Environmental Protection Act, provides that it is illegal to, among other things, "enlarge" an inland lake without a permit from the DEQ. MCL 324.30102(d). However, the then-applicable administrative rule defined the term "enlarge" to include only dredging the bottomlands of a lake to increase its footprint, and did not contemplate adding water to raise the lake level. Mich Admin Code, R 281.811(1)(e).[2]

[2] As set forth earlier in the "Statutes and Regulations" section of this brief, this rule has since been amended and the definition of "enlarge or diminish an inland lake or stream" has been removed. 2015 Michigan Register 5 (April 1, 2015), p 75.

Based on language in a circuit court decision in a prior case, as well as a memorandum of advice from the Department of Attorney General, the DEQ acknowledged that adding water to increase the lake level "enlarges" the lake, and began the process of amending the rule to harmonize it with the statute. The rule was ultimately amended, but this litigation arose before the amendment was effective. As a result, the DEQ was faced with the question of what to do until such time as the rule was amended: require a permit not mandated by the rule, or allow the proposed activity to take place without a permit in violation of the statute.

Relying on the well-established principle that statutes take precedence over rules when the two conflict, the DEQ staff applied the statute rather than the rule, required a permit, and then defended the initial denial of a permit in a contested case hearing. After the DEQ ultimately determined at the conclusion of the first contested case hearing that the well did not require a permit under Part 301, the Lake Board petitioned for attorney fees under the Administrative Procedures Act, MCL 24.323.

In a second contested case proceeding focused on attorney fees, the administrative law judge found that the DEQ's position in the underlying case was not devoid of arguable legal merit or otherwise frivolous and therefore denied attorney fees. On direct appeal, the circuit court reversed that decision. The Court of Appeals granted leave to appeal, reversed the circuit court, and reinstated the administrative decision denying attorney fees.

This Court should deny the Lake Board's application for leave to appeal because the Court of Appeals properly held that: (a) the circuit court applied an incorrect legal standard for the award of attorney fees under MCL 24.323; and (b) the DEQ's position was not devoid of arguable legal merit.

Two different administrative law judges, the Director of the DEQ, and the Court of Appeals all determined that the statute and the rule necessitated opposite results when applied to the facts of this case. When the application of two laws to the same set of facts necessitates the opposite result, that is the very definition of a conflict. And Michigan law has been clear for decades that, in the event of a conflict, it is the statute that controls and not the rule.

Against this regulatory background, the Lake Board's position – that the DEQ was required to *violate a statute* in order to uphold the conflicting rule, and that it was not even an *arguable* legal basis for the DEQ to proceed otherwise – simply does not hold water.

Contrary to the Lake Board's assertions, the Court of Appeals did not hold that DEQ or any other administrative agency is free to disregard promulgated administrative rules. Instead, it narrowly held that, on the facts of this specific case, the administrative law judge did not abuse his discretion, because "DEQ's legal position was sufficiently grounded in law as to have at least some arguable legal merit, and hence it was not 'frivolous' under MCL 24.323(1)(c)."

(Ex A, p 7.) And nothing in the Court of Appeals opinion suggests or supports, as the Lake Board claims, the use of a "subjective" standard for determining whether a legal position has arguable legal merit.

This Court should deny leave to appeal because the Lake Board cannot show that review is warranted under the factors set forth in MCR 7.305(B) for the following reasons.

- This matter does not involve any question, let alone a substantive question, as to the validity of any legislative act.
- While this is a case brought against a state agency, it is not a matter of significant public interest. This matter affects one specific request for attorney fees in one contested case hearing on one lake level project. This is the only time that the conflict between the statute and rule at issue was ever litigated, and the rule has been successfully amended so that the conflict no longer exists. Therefore, it is legally and factually impossible for this issue to arise again.
- This matter does not involve legal principles of major significance to the state's jurisprudence. It involves a limited dispute between the Lake Board and the DEQ as to attorney fees in a unique contested case, and arises from a conflict of laws that no longer exists.
- The decision of the Court of Appeals to reverse the circuit court's opinion and reinstate the decision of the administrative law judge was not clearly erroneous – in fact, it was correct. That decision will not cause any material injustice to any party, nor does it conflict with any prior decisions of this Court or the Court of Appeals, let alone "30 years of well-established case law" as the Lake Board claims. To the contrary, it would cause a material injustice to the DEQ if it was forced to pay attorney fees for adhering to well-established legal principles and not violating an applicable statute.

COUNTER-STATEMENT OF FACTS AND PROCEEDINGS

This matter arises from an opinion and order of an administrative law judge (ALJ) denying the Lake Board's petition for attorney fees under MCL 24.323(1). (Admin Rec Vol 1, pp 8-13.) The Lake Board sought to recover fees incurred in a separate, previous administrative contested case hearing, as well as prior court proceedings in the Oakland Circuit Court and the Court of Appeals.

The ALJ denied the Lake Board's petition for attorney fees, finding that the DEQ's position in the underlying lawsuits was not frivolous. This decision was reversed by the Ingham Circuit Court, and that decision was subsequently reversed (and the ALJ's decision reinstated) by the Court of Appeals.

The Lake Board's initial permit application

On March 12, 2009, the Lake Board applied to the DEQ for a permit pursuant to Part 301, Inland Lakes and Streams, and Part 303, Wetland Protection, of the Natural Resources and Environmental Protection Act, MCL 324.30101 *et seq*. & MCL 324.30301 *et seq*.

The permit application called for placing fill material in a wetland, and placing a rock "riprap" channel in Grass Lake in Oakland County. The riprap channel would carry water from an augmentation well (a structure which draws water out of the ground) into the lake, raising the lake level. (Admin Rec Vol 2, pp 894-907.)

The DEQ denied the Lake Board's application under both Part 301 and Part 303 on the grounds that, "the proposed project would have significant adverse impacts on the natural resources associated with Grass Lake and the wetland areas contiguous to Grass Lake." (Admin Rec Vol 2, pp 909-910.)

The Lake Board filed a petition for a contested case hearing to challenge the permit denial. However, before proceeding with that contested case, the Lake Board filed a complaint for declaratory relief in the Oakland Circuit Court on August 24, 2010. At the Lake Board's request, the parties agreed to hold the contested case hearing in abeyance pending the outcome of the circuit court action. (Admin Rec Vol 2, pp 914-915.)

The Lake Board's complaint for declaratory relief in the Oakland Circuit Court

In the Oakland Circuit Court action, the Lake Board sought a declaration that it was not required to obtain a permit for the proposed project under Part 301 because the definition of "enlarge a lake" in the administrative rule did not include the addition of water to a lake to raise the lake level.

A trial was held in that matter on June 27 and July 22, 2011. The Lake Board called DEQ employees Kim Fish and Melanie Foose (formerly Melanie Skavang) as witnesses.

Ms. Fish, the Assistant Division Chief of the DEQ's Water Resources Division, was called as a witness by the Lake Board because she was involved in the drafting of the DEQ's guidance document on augmentation wells, and because she was involved in the process of revising the DEQ's administrative rules. Ms. Fish testified that she believed that raising the level of an inland lake constituted an enlargement of the lake under the plain language of Part 301. Ms. Fish acknowledged that there was a conflict between the language of the statute and the language of the rule and testified that, when there is a conflict between a statute and a rule, Michigan law dictates that the statute controls. (Admin Rec Vol 1, pp 168 [transcript, p 128:11-14] and 169 [transcript, p 129:19-22].)

Ms. Fish also testified that the DEQ had attempted to change the administrative rule, but that it was unsuccessful in doing so at that point, both because of disagreements among relevant stakeholders and because the United States Environmental Protection Agency was in the process of conducting a multiyear-long audit of the DEQ's delegated water programs, and that this prevented the DEQ from obtaining the necessary approvals to get the rule changed. (Admin Rec Vol 2, pp 640-642 [transcript, pp 129:23-131:24].)

Ms. Foose, who was the DEQ field staff member who reviewed the Lake Board's permit application and issued the denial letter, testified that she made the decision to deny the permit based on the plain language of Part 301, which requires a permit to enlarge a lake. (Admin Rec Vol 1, p 167:6-10.)

On July 22, 2011, at the conclusion of the Lake Board's case in chief, the DEQ brought a motion for directed verdict pursuant to former MCR 2.515,[3] arguing that the Lake Board had failed to establish that it had standing to bring the action, and that the court lacked subject matter jurisdiction over the dispute because the Lake Board had failed to exhaust administrative remedies. The court ordered the parties to submit briefs on the issues of standing and jurisdiction. After briefing was concluded, the court issued its opinion and order on October 17, 2011, granting the DEQ's motion for directed verdict with regard to both standing and subject matter jurisdiction. (Admin Rec Vol 1, pp 170-178.)

The Lake Board appealed the Oakland Circuit Court's opinion and order to the Court of Appeals (Docket No. 306991). On February 14, 2013, the Court of Appeals issued a memorandum opinion and order affirming the circuit court's opinion and order on the issue of jurisdiction and holding that, having decided the matter on the issue of jurisdiction, it did not need to consider the issue of standing. The Court of Appeals further held that the appropriate forum in which to litigate this dispute was in an administrative proceeding. (Admin Rec Vol 1, pp 179-180.)

[3] At the time of the trial, motions for directed verdict were governed by MCR 2.515. In the 2012 Michigan Court Rules, that rule was recodified as MCR 2.516 without any change to the substance of the rule.

Resumption of the original contested case hearing

With the declaratory action and subsequent appeal concluded, the parties returned to the administrative tribunal to resume the contested case hearing regarding the permit denial (which, at that point, had been held in abeyance at the Lake Board's request for over two years).

The parties filed cross-motions for summary disposition on, among other things, the issue of whether the proposed project constituted enlarging a lake and, if so, whether the Lake Board was required to obtain a permit under Part 301. (Admin Rec Vol 2, pp 585-784.)

On July 31, 2012, the presiding ALJ issued an order granting the Lake Board's motion for summary disposition on this issue. The ALJ held that the proposed project did constitute an enlargement of the lake and so a permit would be required under the plain language of the statute, but that the DEQ was obligated to follow its administrative rules and, therefore, could not require the Lake Board to obtain the permit. (Admin Rec Vol 2, pp 569-582.)

The ALJ based this holding on a single sentence of dicta from the Court of Appeals decision in *Micu v City of Warren*, 147 Mich App 573, 584 (1985), which stated that, while statutes take precedence over rules when the two conflict, an agency must change its rule rather than simply ignore it. (Admin Rec Vol 2, p 578.) The ALJ neither addressed the fact that the DEQ had unsuccessfully attempted to change the rule, nor explained how a statement that state agencies cannot ignore an administrative rule means that state agencies can ignore a conflicting statute.

The parties filed written exceptions to the ALJ's decision with the Director of the DEQ pursuant to MCL 24.281(1). In its exceptions, the DEQ pointed out that this Court and the Court of Appeals have held for decades that, when a statute and a rule conflict, the statute controls. (Admin Rec Vol 2, pp 490-514.) The DEQ further argued that it was erroneous for an agency to apply its rule, in violation of a statute, based on one sentence of dicta from one case. (*Id*.) Finally, the DEQ argued that it would be problematic for an agency to essentially declare itself free to violate or ignore the plain language of statutes as long as it first promulgates a rule that conflicts with those statutes. (*Id*.)

On October 11, 2012, the DEQ Director issued an order finding that there were unresolved questions of fact, and that a factual record needed to be created before the parties' cross-motions for summary disposition could be decided, and remanding the matter to the ALJ to conduct an evidentiary hearing. (Admin Rec Vol 2, pp 477-479.)

The parties agreed that the issue of whether the Lake Board was required to obtain a permit for the proposed augmentation well under Part 301 (in other words, whether it was the statute or the rule that controlled) was a purely legal issue for which a factual record did not need to be developed. Therefore, the Lake Board filed a motion for reconsideration, in which the DEQ concurred. (Admin Rec Vol 2, pp 470-473.)

On May 1, 2013, the DEQ Director issued a final order on motion for reconsideration which adopted and incorporated the ALJ's July 31, 2012 order, ruling that the proposed project was not regulated under Part 301 because the DEQ was obligated to apply the administrative rule. (Admin Rec Vol 2, pp 432-437.) This order stated that the DEQ, "does not point to a specific or particular conflict between the statute and the rule. It only cites to a different result in regulating a proposed project when considering it under the Statute [sic] versus the Rule [sic]." (Admin Rec Vol 2, p 435.)

With the Part 301 issues resolved in the Lake Board's favor, the DEQ believed that the primary issue in the case was decided and did not wish to further litigate the remaining Part 303 (wetlands) issues. The DEQ therefore issued a permit to the Lake Board, authorizing the proposed project. After some minor wrangling over whether the specific details of the permit satisfied the Lake Board's application, the DEQ issued an amended permit on June 26, 2013, which addressed the Lake Board's remaining concerns. (Admin Rec Vol 2, pp 365-368.) The Lake Board then filed a motion for summary disposition of the remaining issues in the contested case hearing, in which the DEQ concurred. (Admin Rec Vol 2, pp 336-364.) The ALJ granted the Lake Board's motion for summary disposition on July 17, 2013, resolving the first contested case hearing. (Admin Rec Vol 2, pp 333-335.)

The Lake Board's petition for attorney fees

Having prevailed in the underlying contested case hearing, the Lake Board filed a petition for a second contested case hearing on the issue of attorney fees, from which this application for leave to appeal arises. (Admin Rec Vol 1, pp 240-332.)

The basis of this petition was that Michigan's Administrative Procedures Act (APA), MCL 24.201 *et seq*., provides that a prevailing party in a contested case hearing may seek attorney fees if the agency's position in that contested case was frivolous. An agency's position is "frivolous" under the APA if any of the following apply:

> (a) The agency's primary purpose in initiating the action was to harass, embarrass, or injure the prevailing party.
>
> (b) The agency had no reasonable basis to believe that the facts underlying its legal position were in fact true.
>
> (c) The agency's legal position was devoid of arguable legal merit. [MCL 24.323(1)(a)-(c).]

The APA further provides that attorney fees awarded under this provision are limited to a rate of $75.00/hour unless the "presiding officer" (the ALJ) determines that special circumstances existed justifying a higher rate, or an applicable rule promulgated by the agency provides for the payment of a higher rate because of special circumstances. MCL 24.323(5)(b).

The parties filed cross-motions for summary disposition and multiple briefs in response on the issue of whether the DEQ's position in the previous contested case hearing was frivolous as defined in MCL 24.323(1)(a)-(c). (Admin Rec Vol 1, pp 14-207.)

In its petition and motion filings, the Lake Board alleged that all three of the MCL 24.323(1) factors were present in the underlying contested case, and that the complex nature of the factual issues required extensive scientific expertise which justified an award of attorney fees at rates higher than the amount set forth in MCL 24.323(5)(b). Specifically, the Lake Board argued that, in part because its lead attorney possessed a bachelor's degree in engineering, its team of three attorneys was entitled to fees at rates of $350.00/hour for attorney Charles Dunn, $300.00/hour for attorney Celeste Dunn, and $250.00/hour for attorney John Miller. (Admin Rec Vol 1, p 243.) The Lake Board did not explain why scientific expertise was required to argue a case that the Lake Board itself had previously argued depended entirely on a single legal issue and had no factual component. (Admin Rec Vol 2, pp 470-473.)

The Lake Board also alleged that it was entitled to attorney fees for a total of 377.8 hours spent working on the case, including all of the hours spent working on the declaratory action in the Oakland Circuit Court and the subsequent appeal to the Court of Appeals. (Admin Rec Vol 1, pp 306-316.) To clarify: the Lake Board asked an ALJ to award it attorney fees incurred in *other lawsuits* in *other courts* in which the Lake Board *did not prevail*, and in one of which the Court of Appeals

ordered the Lake Board to pay the DEQ's costs. (Admin Rec Vol 1, pp 179-180.) In total, the Lake Board asked the ALJ to award attorney fees of over $130,000.00 for a contested case hearing that was decided on motions focused on legal, not factual, issues. (Admin Rec Vol 1, p 243.)

The Lake Board also accused the DEQ of, among other things, behaving in a manner that was "nothing short of appalling," "waging an informal campaign" against the Lake Board, and exhibiting "obvious bias" in reviewing the Lake Board's permit application. (Admin Rec Vol 1, p 106.)

The DEQ argued that none of the MCL 24.323(B)(1) factors was present in the underlying contested case hearing, and that the DEQ's position was not frivolous because it was supported by overwhelming case law. (Admin Rec Vol 1, pp 141-146.)

On June 23, 2014, the ALJ issued an order granting the DEQ's motion for summary disposition on the grounds that the DEQ's position in the previous contested case hearing had not been frivolous. (Admin Rec Vol 1, pp 8-13.)

The ALJ specifically found that the DEQ's position was not devoid of arguable legal merit because the legal issues in the underlying contested case hearing were complex. (Admin Rec Vol 1, pp 10-11.) The ALJ also found that there was no evidence that the DEQ's primary purpose in denying the Lake Board's permit application was to harass, embarrass, or injure the Lake Board under MCL 24.323(1)(a). (Admin Rec Vol 1, p 11.) Finally, the ALJ found that there was no factual dispute at issue (as the parties previously agreed), and so the DEQ could not

be deemed to have known that the facts underlying its legal position were untrue under MCL 24.323(1)(b). (Admin Rec Vol 1, p 10.)

The Lake Board's appeal to the Ingham Circuit Court

The Lake Board appealed the ALJ's order to the Ingham Circuit Court pursuant to MCL 24.301. In its appeal, the Lake Board argued only that the DEQ's position in the first contested case hearing was frivolous because it was devoid of arguable legal merit under MCL 24.323(1)(c). It did not appeal the ALJ's determinations with regard to MCL 24.323(1)(a) and MCL 24.323(1)(b).

The parties filed briefs on appeal, and oral argument was held in the circuit court on February 4, 2015. During the argument, the court expressed displeasure with the requirements of the APA and Michigan's administrative laws in general, specifically noting that $75.00/hour is, in the court's opinion, an insufficient rate of fees which an attorney cannot live off of. (2/4/15 Hr'g Tr, p 14:16-24 and p 18:2-18.)

The court then precluded counsel for the DEQ from arguing about the rate of attorney fees, noting that whether "special circumstances" existed which would justify a higher rate as contemplated in MCL 24.323(5)(b) would properly be decided by the ALJ after an evidentiary hearing if the circuit court reversed and remanded. (2/4/15 Hr'g Tr, p 18:2-18.)

On March 3, 2015, the circuit court issued its order, reversing the order of the ALJ. (Ex B.) In its order, the circuit court first held that the ALJ's determination that the DEQ's position in the previous contested case was not devoid of arguable legal merit was arbitrary and capricious because the ALJ "failed to make any conclusions of fact or law." (Ex B, p 3.)

Next, the circuit court held that the DEQ's position in the previous contested case "was frivolous by being devoid of legal merit." (Ex B, p 3.) The circuit court found that there was no direct conflict between the statute and the rule in this case because the DEQ Director had previously questioned whether there was actually a conflict, and because the rule defines the term "enlarge," whereas Part 301 does not. (Ex B, p 4.) The court then held that an administrative agency must follow its own rule and that, here, the DEQ, "knowingly violated its own rule . . . for years without attempting to re-promulgate a new rule. Given the overwhelming case law that condemns this exact behavior, it is clear that reliance on a policy that prescribes that behavior is devoid of legal merit." (Ex B, p 4.)

The court then addressed the rate of attorney fees set forth in MCL 24.323(5)(b) – the very issue that the court forbade counsel for the DEQ from arguing because deciding this issue on appeal would be improper. The court held that "special circumstances do apply in this case, due to the complex matter of the case, which required highly technical understandings of the natural sciences, engineering, and state and federal environmental law." (Ex B, p 4.) The court held that the requested rates (of nearly five times the amount set by statute) were

justified under these special circumstances. (Ex B, p 5.) It ordered that the Lake Board was entitled to recover fees and costs incurred in defending its position in the contested case proceedings in the Michigan Administrative Hearing System at the rates it requested.

The court held that the Lake Board was not entitled to fees and costs incurred defending its position before the Oakland Circuit Court and the Michigan Court of Appeals in Docket No. 306991. (Ex B, p 5.)

Proceedings in the Court of Appeals

After briefing and oral argument, the Court of Appeals issued its order on July 21, 2016, reversing the order of the Ingham Circuit Court and reinstating the decision of the ALJ. (Ex A.) Specifically, the Court of Appeals held that the DEQ's underlying legal position was not frivolous, given the clear tension between the statute and the rule. (Ex A, pp 6-7.) The Court of Appeals further held that the circuit court had applied incorrect legal principles by reviewing the ALJ's decision under the incorrect legal standard. The Lake Board then filed its application for leave to appeal to this Court.

STANDARD OF REVIEW

Whether the DEQ's position in the underlying contested case hearing was devoid of arguable legal merit is a purely legal issue, which this Court reviews *de novo*. *In re Complaint of Rovas*, 482 Mich 90, 102 (2008).

In its application for leave to appeal, the Lake Board inaccurately states the standards of review that the Ingham Circuit Court was supposed to apply in its review of the ALJ's decision. The Lake Board asserts that the circuit court's "task was to review the administrative decision to determine if it was authorized by law and supported by competent, material, and substantial evidence on the whole record." (Lake Board's Application, p 9.) This is incorrect. In an appeal from an ALJ's decision to award or not award attorney fees, the circuit court's task is actually to determine whether "the failure to make an award or the making of an award was an *abuse of discretion*." MCL 24.325(2); *Widdoes v Detroit Pub Sch*, 218 Mich App 282, 289 (1996).

Michigan courts have interpreted "abuse of discretion" as "when the court chooses an outcome that falls outside the range of reasonable and principled outcomes." *People v Unger*, 278 Mich App 210, 217 (2008). Additionally, the Court of Appeals has defined "abuse of discretion" with regard to administrative agency decisions as follows:

> To reverse an administrative agency's decision as an abuse of discretion . . . a court must find the result so palpably and grossly violative of fact and logic that it evidences a perversity of will, a defiance of judgment, or an exercise of passion or bias. *In re Kurzyniec Estate v Michigan Dep't of Social Servs*, 207 Mich App 531, 537 (1994), citing *Marrs v Bd of Med*, 422 Mich 688, 693-694 (1985).

Finally, the Michigan Administrative Hearing System (which employs ALJs to preside over contested case hearings) is the agency charged with applying MCL 24.323(1) to determine whether attorney fees are warranted in contested case hearings. As such, an ALJ's interpretation of MCL 24.323(1) is entitled to respectful consideration by the courts and should not be overturned without cogent reasons. *In re Complaint of Rovas against SBC Michigan*, 420 Mich 90, 103 (2008).

The Lake Board does accurately cite what the standard of review was in the Court of Appeals, though. Specifically, the Court of Appeals reviewed the circuit court's decision to determine whether the circuit court had applied incorrect legal principles, or whether it misapprehended or grossly misapplied the substantial evidence test to the agency's factual findings. (Lake Board's Application, p 9.)

ARGUMENT

I. Given the conflict between the statute and the rule, the DEQ's legal position that it should apply the statute instead of the rule was not devoid of arguable legal merit.

The Court of Appeals correctly recognized the clear conflict between the statute and the rule in this matter. Specifically, the Court of Appeals held that there is "an undeniable tension between the legal rules cited by the parties in the prior contested case," and found that, while an agency may not ignore its own rules, it also may not violate statutes in order to uphold those rules. (Ex A, p 6.)

In its application for leave to appeal, the Lake Board argues that there was no conflict between the statute and the rule. (Lake Board's Application, pp 10-16.) This argument fails for two reasons.

1. There was a conflict between the statute and the rule, because they necessitated opposite results when applied to the set of facts at issue.

First, multiple courts, tribunals, and agencies have concluded that there is a conflict here.

- As set forth earlier, in a prior lawsuit, the Mecosta County Circuit Court admonished the DEQ because its rule conflicted with the plain language of the statute. (Ex H to Lake Board's Application, pp 13-14; 17-18.)

- When the DEQ sought legal advice on this issue in response to the Mecosta County Circuit Court's admonishment, the Department of Attorney General advised the DEQ that a conflict existed.

- In the initial contested case hearing, the ALJ held that a permit was required under the statute, but not under the rule. (Admin Rec Vol 2, pp 569-582.)

- In issuing the final decision and order in that contested case hearing, the DEQ Director questioned whether a conflict existed, but acknowledged that the statute and the rule yield different results here (which is the very definition of a conflict). (Admin Rev Vol 2, p 435.)

- In the second contested case hearing regarding attorney fees, a second ALJ implied the existence of a conflict by holding that the DEQ's position was not devoid of arguable legal merit because of the complexity of the legal issues at play.

- Finally, the Court of Appeals held that there was an "undeniable tension" between the statute and the rule. (Ex A, p 6.)

On the other hand, only the Ingham Circuit Court affirmatively held that there was no conflict at issue here. That holding was based on two things: that the DEQ Director had determined as much in the initial contested case hearing, and that there is no conflict because the rule defines the term "enlarge" whereas the statute does not. (Ex A, p 4.)

The circuit court erred on both counts. First, while the court referred to the DEQ Director's final order in the initial contested case hearing, a review of that order demonstrates clearly that a conflict does, in fact, exist between the statute and the rule. What the Director's final order actually says is that the DEQ "does not point to a specific or particular conflict between the statute and the rule. It only cites to a different result in regulating a proposed project when considering it under the Statute (sic) versus the Rule (sic)." (Admin Rec Vol 1, p 435.)

Simply put, this is the very definition of a conflict. When two laws apply to the same situation, but the application of each law mandates the opposite result, that is a conflict.[4] At a minimum, the DEQ's position in the contested case hearing that the rule conflicted with the statute and that the statute controlled had at least arguable legal merit and was therefore not frivolous.

The court went on to describe the rule as a "narrow interpretation of the statute," and not a direct conflict. (Ex B, p 4.) But an agency cannot interpret a statute so narrowly that it contradicts the plain meaning of the statute. *Ludington Serv Corp v Acting Comm'r of Ins*, 444 Mich 481, 505 (1994); *Fellows v Michigan Comm for the Blind*, 305 Mich App 289, 299-300 (2014).

[4] It appears that there is little, if any, Michigan case law that defines the word "conflict" with respect to conflicts between statutes and administrative rules. However, this Court has applied this principle to jury instructions, referring to conflicting instructions as ones which necessitate different results. *Kirby v Larsen*, 400 Mich 585, 606 (1977). Additionally, the definition of the word "conflict" means, among other things, "To come into opposition; collide; differ." *The American Heritage Dictionary*, p 279 (New College Ed 1976).

As set forth earlier, in the initial contested case hearing, both the ALJ and the DEQ Director found that application of the plain language of the statute necessitated the opposite result of application of the rule. The circuit court's conclusion that this is a "narrow interpretation" that does not rise to the level of a conflict between the statute and the rule is a misapplication of basic legal principles that was properly rejected by the Court of Appeals. Likewise, this Court should reject the Lake Board's argument that there is no tension between the statute and the rule, and that the two can be harmonized. (Lake Board's Application, pp 12-17.) As the Court of Appeals properly determined, the circuit court's reasoning (reiterated by the Lake Board in its application) does not support the conclusion that the DEQ's position was devoid of *arguable* legal merit.

2. Even if there was no conflict between the statute and the rule (which there is), the Lake Board's argument still fails because the DEQ need only show that the existence of a conflict is *arguable*.

The Lake Board's argument also fails because, in order for the DEQ to prevail in this matter, it is irrelevant whether a conflict even actually exists. Rather, the Lake Board's argument fails if it is even *arguable* that a conflict exists.

The DEQ's position was, and remains, that there was a conflict between the statute and the rule. As long as this position has *arguable* legal merit, the DEQ's position is not frivolous. (Ex A, pp 5-7, citing MCL 24.323(1)(c) & *Adamo Demolition Co v Dep't of Treasury*, 303 Mich App 356, 368 (2013).) Given that the Court of Appeals, the Mecosta County Circuit Court (in a prior case), two ALJs, and

the DEQ Director recognized that there was conflict or tension between the statute and the rule, the DEQ's position that there was a conflict is undeniably arguable.[5]

3. Because Michigan law is clear that, when a statute and a rule conflict, the statute controls, it was not frivolous for the DEQ to argue that it should apply the statute until such time as it could amend the rule.

It is a fundamental principle of administrative law that, when a statute and a rule conflict, the statute controls. Michigan Pleading and Practice § 60:26, citing *Michigan Sportservice, Inc v Nims Turfservice, Inc*, 319 Mich 561 (1948); *Guss v Ford Motor Co*, 275 Mich 30 (1936); *Kurtz v Shawley Motor Freight Co*, 270 Mich 112 (1935).

The basis for this principle is that, while the Legislature may delegate rule-making authority to an administrative agency, the agency may not enact rules that exceed the scope of that delegation, because to do so would be to usurp the Legislature's authority to enact laws. *Herrick Dist Library v Library of Michigan*, 293 Mich App 571, 580-584 (2011).

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[5] In its application, the Lake Board accuses the Court of Appeals of applying a "subjective standard to whether a claim more (sic) defense is frivolous." (Lake Board's Application, p 12.) The Lake Board provides no basis for this accusation, and indeed none exists. The DEQ has never argued, and the Court of Appeals did not hold, that any subjective standard is sufficient. Rather, the Court of Appeals properly held that the DEQ's legal position was "sufficiently grounded in law as to have at least some arguable legal merit, and hence it was not 'frivolous' under MCL 24.323(1)(c)." (Ex A, p 7.)

The circuit court's holding that the DEQ's position was devoid of legal merit, and that the ALJ's holding to the contrary was arbitrary and capricious, referred to "overwhelming case law" that condemns the DEQ's behavior, but cited only one case. And that case does not in any way condemn the DEQ's behavior here, let alone establish that the DEQ's position in the contested case was devoid of arguable legal merit. (Ex B, p 4.)

The lone case relied on by the circuit court on this issue was *Micu v City of Warren*, 147 Mich App 573, 584 (1985). In *Micu*, the Court of Appeals held that statutes prevail over rules when the two conflict. (*Id.*) That holding, of course, is fully consistent with the DEQ's argument in the underlying contested case. The Court of Appeals then stated in dicta that agencies must change their rules rather than simply ignore them. (*Id.*) But *Micu* did not hold or even imply that an agency position that a statute take precedence over a conflicting administrative rule lacks arguable legal merit.

The circuit court specifically found that the DEQ not only violated its own rule, but that "it apparently did so for years without attempting to re-promulgate a new rule." (Ex B, p 4.)

As a preliminary matter, this finding was erroneous because the administrative record clearly establishes that the DEQ attempted to amend its rule but was unable to do so at the time.[6] (Admin Rec Vol 2, pp 640-642.) State agencies

[6] As noted above, the rule has since been successfully amended to eliminate the conflict.

cannot simply amend rules whenever they see fit. Rather, when the DEQ first attempted to amend this rule, it was required to follow an extensive procedure set forth in the APA that governs the promulgation and amendment of rules, which requires approval from the Office of Regulatory Reform, followed by public notice and comment periods and hearings, then certification by the Legislative Services Bureau, review by the Legislature's Joint Committee on Administrative Rules, approval by the Legislature and the Governor (if the Joint Committee on Administrative Rules objects to the proposed amendment), and filing by the Secretary of State. MCL 24.239-247. The circuit court's finding that the DEQ never attempted to amend its rule is not supported by any facts in the record, and in fact is directly contradicted by the record. (Admin Rec Vol 2, pp 640-642.)

More substantively, the circuit court did not explain how the Court of Appeals decision in *Micu* authorizes state agencies to ignore the plain language of statutes and violate those statutes until such time as they can change the administrative rules to conform to the statute. In any event, *Micu* does not support the conclusion that the DEQ's position in the contested case was devoid of arguable legal merit and therefore frivolous.

In its application, the Lake Board now argues that the Court of Appeals decision in this matter is "contrary to over 30 years of well-established case law." (Lake Board's Application, pp 17-18.) In support, the Lake Board cites several cases which stand for the proposition that administrative agencies must follow their own rules. (*Id.*) However, this argument fails because the issue here is not whether an

agency must follow its own rules, but whether it is even arguably meritorious for an agency to follow a statute in lieu of a conflicting rule until such time as the rule can be changed.

The narrow, limited issue raised in this case is not addressed in the cases relied upon by the Lake Board. Additionally, in light of the circuit court's legal and factual errors, the Court of Appeals properly held that the circuit court applied incorrect legal principles in holding that DEQ's position was devoid of arguable legal merit where the DEQ relied on well-established case law. (Ex A, pp 5-7.)

II. The Court of Appeals properly concluded that the circuit court applied incorrect legal principles when it relied on an incorrect procedural statute and an incorrect standard of review to reverse the ALJ's decision.

The Court of Appeals held that the circuit court applied incorrect legal principles in part because the circuit court held that the DEQ's underlying position was "devoid of legal merit." (Ex A, p 5.) The circuit court erred because, of course, the standard is whether the DEQ's position was devoid of *arguable* legal merit. (Ex A, p 5.) As set forth earlier, the DEQ's position was clearly at least *arguable*.

Additionally, though the Court of Appeals did not reach this issue, the circuit court reviewed the ALJ's decision under the incorrect procedural statute and, as a result, applied the incorrect standard of review and ultimately reversed the ALJ's decision for not containing provisions that it was not supposed to contain.

In its opinion and order, the circuit court specifically based its decision to reverse the ALJ's decision on the fact that it did not contain findings of fact and conclusions of law. (Ex B, p 3.) The circuit court held that the failure to include findings of fact and conclusions of law rendered the ALJ's decision arbitrary and capricious, and therefore necessitated reversal. (*Id.*) But the statute relied upon by the circuit court, MCL 24.306, does not govern decisions made by ALJs with regard to attorney fees. Rather, it governs final decisions and orders issued by the DEQ Director.

Orders such as the one issued by the ALJ in this case are not required to contain written findings of fact and conclusions of law. Rather, they merely need to contain "written findings" as to the action and "the basis for the findings." MCL 24.323(4). And, as noted in the "Standard of Review" section of this brief, the circuit court may not reverse an ALJ's decision on the grounds that it is "arbitrary and capricious." Rather, the circuit court can only reverse the ALJ's decision on the grounds that it is an "abuse of discretion." MCL 24.325(2); *Widdoes,* 218 Mich App at 289.

Given the extensive errors in the circuit court's order, the Court of Appeals was clearly correct when it reversed on the grounds that the circuit court applied incorrect legal principles.

CONCLUSION AND RELIEF REQUESTED

The Court of Appeals correctly reversed the circuit court and reinstated the decision of the ALJ because the DEQ's position was not devoid of arguable legal merit. Faced with a clear conflict between a statute and a rule – or, at a bare minimum, an *arguable* conflict between a statute and a rule – the DEQ followed the precedent set by decades of binding case law, as well as the advice of its attorneys, and applied the statute until such time as it could change the rule. The DEQ's legal position in this contested case was, as the Court of Appeals found, "sufficiently grounded in law as to have at least some arguable legal merit, and hence . . . not 'frivolous' under MCL 24.323(1)(c)."

Contrary to the Lake Board's grim prophecies, the narrow decision by the Court of Appeals reinstating the administrative law judge's denial of attorney fees on the facts of this case will not result in widespread confusion about the powers of administrative agencies, or otherwise adversely affect the jurisprudence of the State.

The Lake Board has not established grounds for further review by this Court under MCR 7.305(B). Accordingly, the DEQ respectfully requests that this Court deny the Lake Board's application for leave to appeal.

Respectfully submitted,

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Dated: September 29, 2016

LF: Grass Lake Improvement Board MiSC/AG#2009-0033498-G/Brief – in Opposition to Application for Leave to Appeal 2016-09-27

EXHIBIT A

STATE OF MICHIGAN

COURT OF APPEALS

GRASS LAKE IMPROVEMENT BOARD,

Petitioner-Appellee/Cross-Appellant,

v

DEPARTMENT OF ENVIRONMENTAL QUALITY,

Respondent-Appellant/Cross-Appellee.

FOR PUBLICATION
July 21, 2016
9:05 a.m.

No. 326571
Ingham Circuit Court
LC No. 2014-001064-AA

Before: Wilder, P.J., and Murphy and O'Connell, JJ.

WILDER, P.J.

In these cross-appeals arising out of a contested administrative proceeding, the parties appeal from the circuit court's order reversing the decision of an administrative law judge (ALJ) and awarding attorney fees to petitioner, Grass Lake Improvement Board (the Board). We reverse the circuit court and reinstate the decision of the ALJ.

I. FACTUAL BACKGROUND

The attorney fees at issue were incurred in a previous contested case under the administrative procedures act of 1969 (APA), MCL 24.201 *et seq.*, which was initiated by the Board against respondent, Department of Environmental Quality (DEQ). The dispute between the parties arose after the Board filed an application seeking a permit to use an "augmentation well" to pump water into Grass Lake and thereby increase its water level. In June 2009, DEQ denied the Board's application. In response, the Board filed a petition seeking review of DEQ's decision in a contested cas.

The pivotal issue in the contested case was whether the Board's proposed augmentation well would "enlarge" Grass Lake as that term is used in Part 301 of the Natural Resources and Environmental Protection Act (NREPA), MCL 324.30101 *et seq.*, specifically in MCL 324.30102(1) ("Except as provided in this part, a person without a permit from the department shall not do any of the following. . . . Create, *enlarge*, or diminish an inland lake or stream.")

(emphasis added). Part 301 of the NREPA does not define the term "enlarge," but, at the time DEQ denied the Board's application, the Michigan Administrative Code provided[1] a definition at Mich Admin Code, R 281.811(1)(e):

> "enlarge or diminish an inland lake or stream" means the dredging or filling of bottomlands, or the dredging of adjacent shorelands, to increase or decrease a body of water's surface area or storage capacity or the placement of fill or structures, or the manipulation, operation, or removal of fill or structures, to increase or decrease water levels in a lake, stream, or impoundment.

The Board argued that, under the above definition of "enlarge," its proposed activity of raising the water level by constructing an augmentation well did not constitute an enlargement of Grass Lake. Thus, the Board argued, DEQ's denial of the Board's application was improper under the department's own administrative rules.

DEQ responded that, as interpreted by both DEQ and an advisory opinion of our Attorney General's office, "the plain language of the statute [MCL 324.30102(1)] . . . clearly includes adding water to a lake to increase its volume and surface area[.]" DEQ acknowledged that the above interpretation of MCL 324.30102(1) was contrary to Mich Admin Code, R 281.811(1)(e). Nevertheless, citing the well-settled principle that "when a statute and an administrative rule conflict, the statute controls," DEQ argued that, to the extent its administrative rule conflicted with the plain meaning of MCL 324.30102(1), DEQ was required to follow the statute and ignore the rule.

In reply, the Board argued that, under established Michigan law, administrative agencies, such as DEQ, have a duty to follow their own duly promulgated administrative rules. Citing in support *Micu v City of Warren*, 147 Mich App 573; 382 NW2d 823 (1985), the Board further argued that DEQ's duty to follow Rule 281.811(1)(e) extended even to a situation, such as this, where DEQ believed the rule was contrary to the plain meaning of a statute.

After considering the matter, the ALJ decided in the Board's favor, reasoning as follows:

> [DEQ] contends that it "has worked for years to change the existing administrative rule [Rule 281.811(1)(e)], but such changes can take a very long time due to debate amongst the relevant stakeholders as to what should be changed, and how it should be changed, etc." By making this statement, [DEQ] is acknowledging the very reason why it must follow its administrative rules. When [DEQ] is able to ignore its own administrative rule, it is able to create and enforce policy without considering the input and interests of relevant stakeholders. Reconciling stakeholder interests is an important part of the rulemaking process. Allowing [DEQ] to circumvent its rules through an alternate interpretation bypasses the steps which were created in the APA to account for and protect

[1] Mich Admin Code, R 281.811 has since been amended to remove the definition at issue here. 2015 Mich Reg 5, p 75 (April 1, 2015).

> relevant stakeholders and public interests. The statutory language taken on its own seems broad enough to include the [Board]'s proposed activity (i.e. lake enlargement). However, the rule defining the term "enlargement" clearly limits the [DEQ]'s jurisdiction to activities taking place on bottomlands. Based upon the application of the Rule . . . and other documentary evidence submitted, the proposed lake augmentation project does not implicate Part 301 jurisdiction.
>
> I conclude as a matter of law that the proposed lake augmentation project, that is the act of adding water to the lake without activity on bottomlands, does not implicate the Department's jurisdiction under Part 301. There is no enlargement of Grass Lake.

Following a motion for reconsideration, the ALJ's opinion and order was adopted by DEQ Director Dan Wyant. Thereafter, the remaining issues were summarily dismissed by stipulation of the parties, the contested case was concluded, and DEQ issued the requested permit to the Board.

Afterwards, the Board initiated a second contested case, in which it sought its attorney fees related to the first contested case. Relevant to this appeal, the Board argued that, under MCL 24.323(1), it was entitled to such fees because DEQ's legal position in the prior contested case was "devoid of arguable legal merit." The ALJ denied the Board's request for attorney fees, deciding that DEQ's legal position had at least *some* arguable legal merit:

> Entitlement to relief under § 123(1)(c) may [] be summarily eliminated based on the [Board]'s argument, that "[t]his case is one that has numerous complex legal and technical issues." In reviewing the proceedings and pleadings in this case, the [Board]'s characterization of the "numerous complex legal . . . issues," is accurate. Given this, [DEQ]'s positions cannot be deemed to be devoid of arguable legal merit under MCL 24.323(1)(c).

The Board appealed in the circuit court, which reversed the ALJ's fee decision:

> The ALJ below found that [DEQ]'s position was not devoid of arguable legal merit. . . . The [Board] argues, and this [c]ourt agrees, that this determination fails as a reasoned determination by an administrative agency. The ALJ failed to make any conclusions of fact or law. The ALJ failed to point out any particulars within the record to support such a conclusion. He cited no legal authority and provided no reasoning whatsoever in support of his conclusion. This is the very definition of arbitrary and capricious: unreasoned, without reference to guiding principles or considerations, and a decisive exercise of will or caprice.
>
> Furthermore, [the Board] argues that [DEQ]'s position was frivolous by being devoid of legal merit. This [c]ourt agrees. The [DEQ]'s position was that there existed a conflict of law between a statute, Part 301[of the NREPA], and an administrative rule, [] Rule 281.811. The [DEQ] argued that where such conflicts exist, the statute prevails over the rule[.]
>
> * * *

> However, [] Director [Wyant] found in his final order that . . . the language of the statute and the language of the Rule were not conflicting per se. The statute at issue does not define what it means to "enlarge" a lake or stream, where that is precisely what the Rule does. The Rule's narrow interpretation of the statue is not a direct conflict.
>
> Furthermore, Michigan case law makes it clear that administrative agencies must follow their own rules once properly promulgated. *MICU*[, 147 Mich App at 584]. . . . Here, not only did [DEQ] knowingly violate its own rule, it apparently did so for years without attempting to re-promulgate [sic] a new rule. Given the overwhelming case law that condemns this exact behavior, it is clear the reliance on a policy that prescribes that behavior is devoid of legal merit, and therefore, the [DEQ]'s position in this case was frivolous. This [c]ourt grants [the Board]'s motion for fees and costs incurred defending its case in the Michigan Administrative Hearing System.

The instant cross-appeals followed.

II. STANDARDS OF REVIEW

We review the circuit court's decision to determine whether it "applied correct legal principles and whether it misapprehended or grossly misapplied the substantial evidence test to the agency's factual findings." *City of Sterling Heights v Chrysler Group, LLC*, 309 Mich App 676, 681; 873 NW2d 342 (2015) (quotation marks and citation omitted). We review the circuit court's interpretation and application of statutes de novo. *Glenn v TPI Petroleum, Inc*, 305 Mich App 698, 702; 854 NW2d 509 (2014). On the other hand, an administrative agency's statutory interpretation is reviewed under the standard first enunciated in *Boyer-Campbell Co v Fry*, 271 Mich 282; 260 NW 165 (1935):

> [T]he construction given to a statute by those charged with the duty of executing it is always entitled to the most respectful consideration and ought not to be overruled without cogent reasons. However, these are not binding on the courts, and [w]hile not controlling, the practical construction given to doubtful or obscure laws in their administration by public officers and departments with a duty to perform under them is taken note of by the courts as an aiding element to be given weight in construing such laws and is sometimes deferred to when not in conflict with the indicated spirit and purpose of the legislature. [*In re Complaint of Rovas*, 482 Mich 90, 101, 108; 754 NW2d 259 (2008) (second alteration in original), quoting *Boyer-Campbell*, 271 Mich at 296-297 (quotation marks and citations omitted).]

"Respectful consideration" of an agency's statutory interpretation is not akin to "deference," at least as that "term is commonly used in appellate decisions" today. *Rovas*, 482 Mich at 108. While an agency's interpretation can be a helpful aid in construing a statutory provision with a "doubtful or obscure" meaning, our courts are responsible for finally deciding whether an agency's interpretation is erroneous under traditional rules of statutory construction. *Id.* at 103, 108-109.

III. ANALYSIS

On appeal, DEQ argues that the circuit court applied incorrect legal principles when it reversed the ALJ's decision. We agree.

In pertinent part, MCL 24.323 provides:

> (1) The presiding officer that conducts a contested case shall award to a prevailing party, other than an agency, the costs and fees incurred by the party in connection with that contested case, *if the presiding officer finds that the position of the agency to the proceeding was frivolous*. To find that an agency's position was frivolous, the presiding officer shall determine that *at least 1* of the following conditions has been met:
>
> > (a) The agency's primary purpose in initiating the action was to harass, embarrass, or injure the prevailing party.
> >
> > (b) The agency had no reasonable basis to believe that the facts underlying its legal position were in fact true.
> >
> > (c) *The agency's legal position was devoid of arguable legal merit.*
>
> (2) If the parties to a contested case do not agree on the awarding of costs and fees under this section, a hearing shall be held if requested by a party, regarding the awarding of costs and fees and the amount thereof. . . . [Emphases added.]

Under MCL 24.325(1), "a party that is dissatisfied with the final action taken by the presiding officer under section 123 [MCL 24.323] in regard to costs and fees may seek judicial review of that action pursuant to chapter 6." The reviewing court "may modify" the presiding officer's "action only if the court finds that the failure to make an award or the making of an award was an abuse of discretion, or that the calculation of the amount of the award was not based on substantial evidence." MCL 24.325(2); *Widdoes v Detroit Pub Sch*, 218 Mich App 282, 289; 553 NW2d 688 (1996). If the reviewing court "awards costs and fees to a prevailing party upon judicial review of the final action of a presiding officer in a contested case," then the reviewing court "shall award those costs and fees provided for in [MCL 24.323], if the court finds that the position of the state involved in the contested case was frivolous." MCL 600.2421d; *Widdoes*, 218 Mich App at 289.

The circuit court decided that, under MCL 24.323(1)(c), DEQ's legal position in the original contested case was frivolous. In reaching that conclusion, the circuit court applied an incorrect legal standard. The circuit court reasoned that, because DEQ's legal position was "devoid of legal merit," it necessarily followed that DEQ's legal "position in this case was frivolous." But whether an argument has "legal merit" is not the proper legal question to be considered by the circuit court. Rather, the standard, as announced by MCL 24.323(1)(c), is whether DEQ's legal position "was devoid of *arguable* legal merit." (Emphasis added.)

There is little authority interpreting the language of MCL 24.323(1)(c). Fortunately, however, there are many cases interpreting the nearly identical language found in MCL

600.2591(3)(a).[2] See, e.g., *Adamo Demolition Co v Dep't of Treasury*, 303 Mich App 356, 368; 844 NW2d 143 (2013). We find such authority highly persuasive here. "A claim is not frivolous merely because the party advancing the claim does not prevail on it." *Id.* Instead, "a claim is devoid of *arguable* legal merit if it is not sufficiently grounded in law or fact, such as when it violates basic, longstanding, and unmistakably evident precedent." *Id.* at 369 (quotation marks, citations, and footnotes omitted; emphasis added).

Here, although DEQ did not prevail in the prior contested case, its legal position was sufficiently grounded in law as to have some *arguable* legal merit. There is an undeniable tension between the legal rules cited by the parties in the prior contested case. On one hand, as DEQ argued below, it has long been recognized by Michigan Courts that, due to the very nature of an administrative agency's rulemaking power, when a statute and an administrative rule conflict, the statute necessarily controls. See *Rovas*, 482 Mich at 98 ("While administrative agencies have what have been described as 'quasi-legislative' powers, such as rulemaking authority, these agencies cannot exercise legislative power by creating law or changing the laws enacted by the Legislature."); *Mich Sportservice v Nims*, 319 Mich 561, 566; 30 NW2d 281 (1948) ("The provisions of the rule must, of course, be construed in connection with the statute itself. In case of conflict, the latter governs. It is not within the power of the department of revenue to extend the scope of the act."); *Acorn Iron Works v Auditor Gen*, 295 Mich 143, 151; 294 NW 126 (1940) ("The state board of tax administration from time to time has changed its construction and method of enforcing the sales tax law as it affects building trade transactions; but in this connection it is sufficient to note that liability for payment of the sales tax is controlled by statute. It cannot be imposed by rulings or regulations of the board."); *Walgreen Co v Macomb Twp*, 280 Mich App 58, 71; 760 NW2d 594 (2008) ("A rule is invalid when it conflicts with the provisions of the governing statute.").

On the other hand, it is equally well-settled, as the Board argued below, that agencies are bound to follow their own duly promulgated rules. See *Detroit Base Coalition for Human Rights of Handicapped v Dep't of Social Services*, 431 Mich 172, 189; 428 NW2d 335 (1988) ("An agency is under a duty to follow its own rules."); *Micu*, 147 Mich App at 584 ("[O]nce promulgated, the rules made by an agency to govern its activity cannot be violated or waived by the agency that issued the rules."); *Rand v Civil Serv Comm*, 71 Mich App 581, 586; 248 NW2d

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[2] MCL 600.2591(3)(a) provides:

> (a) "Frivolous" means that at least 1 of the following conditions is met:
>
> (*i*) The party's primary purpose in initiating the action or asserting the defense was to harass, embarrass, or injure the prevailing party.
>
> (*ii*) The party had no reasonable basis to believe that the facts underlying that party's legal position were in fact true.
>
> (*iii*) The party's legal position was devoid of arguable legal merit.

624 (1976) ("An administrative agency, in addition to following constitutional and statutory mandates, must also comply with its own rules.").

Given the tension between such precedents as they apply to the facts of the prior contested case, we conclude that the ALJ did not clearly abuse his discretion. DEQ's legal position was sufficiently grounded in law as to have at least some arguable legal merit, and hence it was not "frivolous" under MCL 24.323(1)(c).[3]

Accordingly, we reverse the circuit court and reinstate the decision of the ALJ. As the prevailing party, DEQ may tax costs pursuant to MCR 7.219.

/s/ Kurtis T. Wilder
/s/ William B. Murphy
/s/ Peter D. O'Connell

[3] Having reached that conclusion, we need not address the additional issues raised in the parties' cross-appeals regarding the propriety of the *amount* of costs and attorney fees awarded by the circuit court.

EXHIBIT B

STATE OF MICHIGAN
IN THE 30TH JUDICIAL CIRCUIT FOR INGHAM COUNTY

GRASS LAKE IMPROVEMENT BOARD,

Petitioner,

v

MICHIGAN DEPARTMENT OF ENVIRONMENTAL QUALITY,

Respondents.

ORDER

CASE NO. 14-1064-AA

HON. WILLIAM E. COLLETTE

At a session of said Court
held in the city of Mason, county of Ingham,
this 31st day of March, 2015.

PRESENT: HON. WILLIAM E. COLLETTE

This matter comes before the Court on Grass Lake Improvement Board's (Petitioner) claim of appeal from a final order by the Michigan Department of Environmental Quality (Respondent) denying Petitioner's request of attorney fees and costs under MCL 24.323. This Court, being fully apprised of the premises, GRANTS Petitioner's motion as to costs and fees incurred in the Michigan Administrative Hearing System, and DENIES Petitioner's motion as to costs and fees incurred in the Oakland County Circuit Court and Michigan Court of Appeals.

FACTS

Petitioner petitioned the Respondent for costs and attorney fees under MCL 24.323 following a lengthy dispute over Petitioner's application for regulatory permission to raise the water level of Grass Lake using an augmentation well. That application resulted in a denial by the Water Resources Division (WRD) and subsequent appeal to

the Oakland County Circuit Court. The circuit court found it did not have jurisdiction to try the case and the Michigan Court of Appeals upheld that decision.

Petitioner moved forward in the Michigan Administrative Hearing System, filing a motion for summary disposition. The Administrative Law Judge granted Petitioner's motion. After several additional motions, a remand by the Director for development of a factual record, and motion for reconsideration by Petitioner, the Director issued a final order granting Petitioner's application in full and holding that Rule 281.811(e) was properly promulgated and is binding.

Petitioner subsequently brought this action for costs and attorney fees under MCL 24.323. The ALJ in that hearing denied Petitioner's motion for disposition and granted instead the WRD's motion for summary disposition. This appeal followed.

STANDARD OF REVIEW

The Administrative Procedures Act provides:

> Except when a statute or the constitution provides for a different scope of view, the court shall hold unlawful and set aside a decision or order of an agency if substantial rights of the petitioner have been prejudiced because the decision or oder is any of the following:
>
> . . .
>
> (e) Arbitrary, capricious, or clearly an abuse or unwarranted exercise of discretion.

A decision is arbitrary if it is "[W]ithout adequate determining principle .... Fixed or arrived at through an exercise of will or by caprice, without consideration or adjustment with reference to principles, circumstances, or significance, . . . decisive but unreasoned." *Goolsby v City of Detroit*, 419 Mich 361, 378; 358 NW2d 856 (1984) (citing *United States v Carmack*, 329 US 230, 243; 67 S Ct 252 (1946)).

ANALYSIS

MCL 24.323 provides that costs shall be awarded to a prevailing party in a contested case if the presiding officer finds the proceeding was frivolous. In order to find that an agency's position was frivolous, the presiding officer must find that the agency's position was intended to harass, embarrass, or injure the prevailing party, that the agency had no reasonable basis to believe that facts underlying its position were true, or that the agency's position was devoid of arguable legal merit.

Petitioner argues that the ALJ's position was arbitrary and capricious. The ALJ below found that the WRD's position was not devoid of arguable legal merit because the WRD alleged that the case had "numerous complex legal and technical issues" based on his review of the record. The Petitioner argues, and this Court agrees, that this determination fails as a reasoned determination by an administrative agency. The ALJ failed to make any conclusions of fact or law. The ALJ failed to point out any particulars within the record to support such a conclusion. He cited no legal authority and provided no reasoning whatsoever in support of his conclusion. This is the very definition of arbitrary and capricious: unreasoned, without reference to guiding principles or considerations, and a decisive exercise of will or caprice.

Furthermore, Petitioner argues that the WRD's position was frivolous by being devoid of legal merit. This Court agrees. The WRD's position was that there existed a conflict of law between a statute, Part 301, Inland Lakes and Streams, of the Michigan Natural Resources and Environmental Protection Act, MCL 324.0101 *et seq.*, and an administrative rule, Michigan Administrative Code Rule 281.811. The WRD argued that where such conflicts exist, the statute prevails over the rule, which was addressed by the

Mecosta County Circuit Court in 2003 in *Michigan Citizens for Water Conservation v Nestle Waters North America, Inc.*, 2003 WL 25659349 Mich Cir Ct, Nov. 25, 2003.

However, the Director found in his final order that the *Nestle Waters* decision did not constitute guidance for the WRD and its future interpretation of Part 301, primarily because the language of the statute and the language of the Rule were not conflicting per se. The statute at issue does not define what it means to "enlarge" a lake or stream, where that is precisely what the Rule does. The Rule's narrow interpretation of the statute is not a direct conflict.

Furthermore, Michigan case law makes it clear that administrative agencies must follow their own rules once properly promulgated. *MICU v City of Warren,* 147 Mich App 573, 584; 382 NW2d 823 (1985). The Director pointed out that "[ev]en if the rule is inconsistent with the statute, an agency must change its rule before acting counter to it." Here, not only did the Respondent knowingly violate its own rule, it apparently did so for years without attempting to re-promulgate a new rule. Given the overwhelming case law that condemns this exact behavior, it is clear the reliance on a policy that prescribes that behavior is devoid of legal merit, and therefore, the WRD's position in this case was frivolous. This Court grants Petitioner's motion for fees and costs incurred defending its case in the Michigan Administrative Hearing System.

MCL 24.323(5)(b) limits available attorney fees to a rate of $75/hour absent special circumstances justifying a higher rate. Petitioner argues that special circumstances do apply in this case, due to the complex matter of the case, which required highly technical understandings of the natural sciences, engineering, and state and federal environmental law. Furthermore, the Petitioner provided a justification for how it arrived

at the figures requested, relying on financial statistics published by the State Bar and requesting figures in line with the 75th percentile hourly rate. This Court finds the requested rates to be reasonable and justified under the special circumstances of the complexity of this case and the frivolity of the WRD's position.

Under MCL 24.323, fees and costs are limited to the contested case in which Petitioner was the prevailing party. Therefore, the Oakland County Circuit Court action and the appeal to the Michigan Court of Appeals are not recoverable.

THEREFORE IT IS ORDERED that the ALJ's Decision is **REVERSED** and Petitioner is **ENTITLED** to fees and costs incurred defending its position in the Michigan Administrative Hearing System at the rates requested.

IT IS ALSO ORDERED that the Petitioner is **NOT ENTITLED** to fees and costs incurred defending its position before the Oakland County Circuit Court and the Michigan Court of Appeals, docket no. 10-112854-CZ.

Hon. William E. Collette
Circuit Court Judge